



**APPROVED MINUTES**  
**APPROVED 03-18-13**  
**CITY OF SCOTTSDALE**  
**AUDIT COMMITTEE**

**MONDAY, FEBRUARY 4, 2013**

**CITY HALL**  
**KIVA CONFERENCE ROOM**  
**3939 NORTH DRINKWATER BOULEVARD**  
**SCOTTSDALE, AZ 85251**

**REGULAR MEETING**

**PRESENT:** Vice Mayor Suzanne Klapp, Chair  
Councilman Robert Littlefield, (arrived at 4:04 p.m.)  
Councilwoman Linda Milhaven,

**STAFF:** Dan Worth, City Manager's Office  
David Smith, City Treasurer's Office  
Jennifer Bowley, Community & Economic Development Division  
Brian Dygert, Community & Economic Development Division  
Paul Katsenes, Community & Economic Development Division  
Don Meserve, Community & Economic Development Division  
Joyce Gilbride, Finance & Accounting Division  
Alan Rodbell, Public Safety Division  
Mel Galbraith, Public Works Division  
Kyla Anderson, City Auditor's Office  
Lai Cluff, City Auditor's Office  
Cathleen Davis, City Auditor's Office  
Joanna Munar, City Auditor's Office  
Sharron Walker, City Auditor's Office

**GUESTS:** Beth Duckett, Arizona Republic

**CALL TO ORDER**

Chair Klapp called the meeting to order at 4:03 p.m.  
A formal roll call confirmed the presence of Committee Members as noted above.

**1. Approval of Minutes, Regular Meeting, November 19, 2012**

**COUNCILWOMAN MILHAVEN MOVED TO APPROVE THE MINUTES OF THE NOVEMBER 19, 2012 REGULAR MEETING. CHAIR KLAPP SECONDED THE MOTION, WHICH CARRIED BY A VOTE OF TWO (2) TO ZERO (0). COUNCIL MEMBER LITTLEFIELD WAS NOT YET PRESENT.**

**2. Discussion and possible direction to staff regarding Sunset Reviews: Historic Preservation Commission**

Councilman Littlefield arrived. City Auditor Sharron Walker introduced the report on the Historic Preservation Commission, noting that the Audit Committee is to make a recommendation to City Council whether to continue or terminate the Commission. She noted that Mr. Don Meserve was in attendance representing the Historic Preservation Commission.

Councilwoman Milhaven thanked Mr. Meserve for his report, noting it is helpful to know what the commission is working on in the upcoming year and to see their value. Chair Klapp thanked Mr. Meserve for the interesting, comprehensive report.

**CHAIR KLAPP MADE A MOTION TO RECOMMEND TO CITY COUNCIL THAT THE HISTORIC PRESERVATION COMMISSION CONTINUE. SECONDED BY COUNCILMAN LITTLEFIELD, THE MOTION CARRIED BY A UNANIMOUS VOTE OF THREE (3) TO ZERO (0).**

**3. Discussion and possible direction to staff regarding Audit Report No. 1303, Cash Handling Control and Accountability**

Ms. Cathleen Davis of the City Auditor's Office said the audit was performed to determine accountability for the City's cash handling, including compliance with related administrative regulations. Staff conducted unannounced cash counts at seven locations in the Community Services, Public Works and Public Safety divisions. For FY 2011/2012, staff throughout the City collected approximately \$440 million for various fines, fees, services and products. About 78 percent of these payments were in check form, 17 percent through wires, electronic fund transfers or interactive voice response, 4 percent through credit or debit card transactions, and only about one percent in cash.

This audit had two findings.

- Some locations reviewed can improve certain aspects of their cash handling practices, such as including documentary supervisor reviews, more limited access to cash drawers and safes, and proper separation of responsibilities to lessen the risk of theft, loss, or fraud.
- Finance and Accounting can improve adherence to certain AR requirements by ensuring the division annually trains City cashiers, performing the required cash handling verifications on an unannounced basis, and clarifying the requirement for timely petty cash reconciliations. In addition, the division should more formally

issue and monitor the use of official manual receipts, explore alternatives for petty reimbursement checks and annually review granted AR exceptions to determine whether a continued business reason exists.

Ms. Davis noted that staff from the Public Works, Public Safety and Finance & Accounting divisions were in attendance.

#### **4. Discussion and possible direction to staff regarding Audit Report No. 1304, WestWorld Financial Operations**

Ms. Kyla Anderson of the City Auditor's Office reviewed the audit report on WestWorld Financial Operations. The audit found that while WestWorld revenues have increased over the last five years, they have covered only 73 to 89 percent of direct operating costs. As a result, the City's General Fund subsidized WestWorld's operating loss of \$335,000 to \$878,000 in each of the last five years. WestWorld's direct expenses decreased by 1.3 percent over the last five years. In contrast, the City's General Fund budget decreased by 23 percent. The Tony Nelssen Equestrian Center's current expansion will enclose and climate control the facility. Management projects the resulting increased events will generate revenue sufficient to pay the associated annual debt service on the MPC bonds approved to fund the expansion.

The audit analyzed WestWorld's financial control, processes and record keeping, seeking to identify ways to help improve its operating results. Based on the audit, WestWorld has opportunities to increase revenues and decrease expenses as well as gain potential operating efficiencies. Additionally two signature event agreements are outdated and modified on an ad hoc basis. Internal controls over invoicing and payment remittance functions can be improved and savings may be achieved in WestWorld's BOR administrative fees, and trailhead costs.

Ms. Lai Cluff of the City Auditor's Office reviewed report details regarding revenues:

- The revenue analysis shows that rates for variable cost services do not recover their associated direct costs.
- Arena rental rates do not recover all direct fixed costs and are below market average pricing.
- The feed and bedding operation, brought in-house in July 2008, netted approximately \$39,000 in FY 2011/2012. The prior third party provided from \$71,000 to \$86,000 in revenues, but WestWorld did not have sufficient control to provide assurance that the City received all applicable user fees from the contract.
- WestWorld may not be collecting all the concession fees due from event concessionaires.
- WestWorld's operational statistics do not accurately monitor actual facility use compared to available capacity. For FY 2011/2012 WestWorld reported a 71 percent occupancy rate, or almost full capacity, based on management's benchmark. However, when monitoring usage as a percentage of available capacity, equestrian facilities achieved a 49 percent occupancy rate during the

- fiscal year. While use days indicate that the facility is near the expected maximum, the capacity use statistics indicate additional room for event growth.
- WestWorld cannot be certain all required ticket surcharge fees were remitted for the Basin Management Fund, since the fee amount is based on self-reported ticket sales.

And Ms. Anderson noted that opportunities exist to reduce certain expenses:

- WestWorld's management projections for the TNEC expansion included labor cost increases of only 4.4 percent through FY 2014/2-15. However this projection may have already been exceeded in the current fiscal year because of salary increases totaling five percent of payroll.
- In addition WestWorld has maintained a full-time staff of about 17 people year round although no events were scheduled in June and July and only three or four small events were scheduled in May and August. During the busier event season more than 14 additional positions are staffed.
- Financial information provided to Council did not include all associated costs. The omitted amounts represent a substantial increase in WestWorld related costs. Facilities maintenance costs, normally part of the City-wide overhead allocation, were included in the March 20, 2012 report, while other overhead costs were omitted.
- Estimated facilities maintenance costs were much higher than they would have been if based on the usual calculation methodology. For FY 2011/2012, WestWorld's actual direct costs totaled \$3.1 million, but with indirect and City wide overhead costs, totaled almost \$6 million.
- Utility costs are not being accounted for consistently.
- Future direct operating costs and debt service payments associated with TNEC would not be recovered by estimated revenues from events secured as of December 2012.

Ms. Cluff discussed simplified rate structures:

- WestWorld uses detailed rates for buildings, facilities and labor, which results in time-consuming detailed tracking and invoicing procedures.
- Event users have expressed dissatisfaction with not knowing their event costs in advance. Combining similar portions of flat fees could both simplify the customer cost estimate and billing process and spread costs among users more equitably.
- Two of WestWorld's three signature events have license agreements that were not originally approved by City Council and do not currently have up-to-date terms. Existing agreement terms allow the event producers to submit letters annually without any action by the City.
- After the multi-purpose tent was added, rather than updating the agreement, the WestWorld management and Barrett-Jackson representatives met to negotiate a new daily base fee and other modifications. It does not appear that other appropriate participants were involved in the license negotiation. The negotiated rates were not formalized in writing and submitted for City Council approval.
- The Sun Country agreement has not been updated and presented for City Council approval, although modifications have been occasionally negotiated.

Ms. Anderson addressed internal controls over revenues:

- WestWorld's procedures for billing, receiving payments and record keeping do not ensure that all revenues are properly reported.
- The auditors found possible failings in WestWorld's BOR administrative fees and trailhead costs. Because WestWorld is located on BOR land, the City's agreement with the BOR affects some costs and revenues. The City would have saved almost \$37,000 in fees over the last four years had the annual increases been limited to the CPI.
- WestWorld maintains a public trailhead site but does not recover the associated costs from the Basin Management Fund. The Fund is restricted to use for BOR land maintenance and improvements and may allow reimbursement of certain trailhead costs.

Ms. Anderson stated that Ms. Jennifer Bowley and Mr. Brian Dygert of WestWorld were in attendance, as was Mr. Paul Katsenes of the Community and Economic Development Division.

Councilwoman Milhaven asked if the analysis included the fee increases approved when Council authorized the TNEC expansion. Staff said the analysis is based on current fees for FY 2012/2013, which include the increases Council approved.

Councilwoman Milhaven asked why the WestWorld plan says that the facility does not have to recover costs. Councilman Littlefield said WestWorld is not an enterprise fund and has consistently lost money for the City. The belief is that the shows at WestWorld are good for tourism. The two goals of the TNEC expansion are (1) to be able to attract summertime events, and (2) to make WestWorld self-sufficient. He opined that the Barrett-Jackson Classic Car Auction receives a very good deal.

Councilwoman Milhaven asked why the City would not recover the full costs of the feed and bedding operation. Mr. Dygert said the cost of manure handling is always a large expense. The biggest challenge at the moment is fuel prices. WestWorld has to contract with a commercial composter, and the hauling expenses costs move unpredictably so he cannot pass them on to the event producers. Management's full intent is to keep manure handling costs to a minimum. Mr. Katsenes added that rates and fees have been steadily increased across the board for the past two years.

Councilwoman Milhaven asked for more details about the manure handling contract. Mr. Dygert said the contract is for volume and contains a fuel surcharge. He cannot predict what the actual fees will be next year. Councilwoman Milhaven suggested passing the hauling bills on to event organizers; Mr. Dygert responded that it would be an option. Chair Klapp asked him if they will be discussing this with Finance & Accounting. Mr. Dygert said they will. Councilwoman Milhaven said with the current TNEC expansion the City should re-evaluate the extent to which it is prepared to subsidize WestWorld. She pointed out that items of this nature are a hidden support to the events. Councilman Littlefield pointed out that the goal is to bring in enough business that the City will not be subsidizing the facility. Councilwoman Milhaven said the City is not recovering its costs and has to service the bond debt for the TNEC expansion.

Ms. Walker said the auditors did the analysis from the standpoint that what was presented to Council was a projection that there would be enough additional events to

cover direct costs and the cost of debt service. So the auditors looked at direct costs, division overhead costs, and City wide overhead costs to lay out a full cost model. With full information, Council can look at striking a balance between recovering costs and staying within market rates. She added that there is not an easy answer. Mr. Dygert is working to generate more activities at WestWorld.

Councilwoman Milhaven said Council might decide to cover a portion of the fixed costs, but she does not feel they should be subsidizing the variable costs without making a conscious decision. She asked the WestWorld staff if they agree with the auditors' projections.

Mr. Dygert said the auditors have not looked into what WestWorld staff is doing and do not know what is in the contract pipeline. Ms. Walker commented that the auditors obtained the list of events known as of December 2012 but would not know details of events developed more recently than that.

In reply to a question by Chair Klapp, Mr. Katsenes said he is in discussions with the City Manager's Office to bring in a marketing consultant. The Purchasing Department is managing the process. They are waiting to hear the evaluation panel's recommendation within the next week or so.

Chair Klapp inquired about WestWorld's policy on deposits. Staff confirmed that for equestrian events, a deposit of 50 percent is required with the balance billed after the event. Chair Klapp noted that the auditors found that many facilities require the entire payment to be made prior to the event. Ms. Walker said one possibility would be to charge the entire facilities fee ahead of time and bill the producer for variable fee items after the event. Chair Klapp urged staff to consider collecting more of the fees for equestrian events before the events take place.

Councilman Littlefield asked if there are any collection issues. Mr. Dygert said there was one in the five years he has worked at WestWorld. Ms. Bowley added there have been a total of seven since 1998. Chair Klapp said in her retail business experience she has learned to get the money up front. Ms. Walker said the recent loss was fairly large; also it is common practice in events management to require more of the money up front.

Councilman Littlefield commented that Council had the same discussion related to WestWorld.

Councilwoman Milhaven commented that if there is a loss on every event, more events would mean bigger losses, which is why it is so important to get a handle on the costs. The fee comparison in the auditor's report shows that most WestWorld pricing is below cost and the market average. She asked why.

Mr. Dygert said he is speculating, based on historical information he has read and gathered through his time with the facility, that WestWorld's fees have been predominantly driven by the users that helped it evolve to where it is now. He has used industry norms in his negotiations with the Bureau of Reclamation. As General Manager, he has been trying to specifically move those rates and fees slowly up to where the industry is, while being sensitive to users. They plan to continue this approach. Some local events will never be able to afford to use the TNEC, but there is still an affordable arena on site. The WestWorld covered arena rates are way below national market rates.

Councilwoman Milhaven asked if the national market rates are increasing faster than the WestWorld rates are rising. Mr. Dygert said in his opinion the national average is not increasing that fast.

Councilwoman Milhaven said a follow-up on this report is needed sooner rather than later. There are so many policy implications in the report. Ms. Walker said the auditors have a follow-up process but WestWorld could be added to the schedule for next year to be covered in more depth. Councilwoman Milhaven suggested that perhaps the WestWorld Subcommittee could review the audit report, with regard to policy implications. While some of the findings can appropriately be reviewed by the auditors, something more needs to be done to consider all the policy implications.

Councilman Littlefield said questions about policy would be a question for the City Council and could be agendaized for discussion at a Council meeting. Councilwoman Milhaven and Chair Klapp both felt that it was preferable to have a discussion at the subcommittee level. Chair Klapp suggested the Auditor could report back with a follow up more quickly than typical. Councilman Littlefield said that Councilwoman Milhaven's concerns are not really audit concerns. She agreed and noted that the budget presented to Council will not show a great level of detail in that regard. Speaking as a long-term member of the WestWorld Subcommittee, Councilman Littlefield said the subcommittee considered all the issues when they updated the WestWorld Master Plan. He commented that when Council approved the TNEC expansion, it was with the understanding that the only way WestWorld could become self-sufficient was to attract more events. The Committee discussed the organization of Council subcommittees for 2013. Chair Klapp said any questions about WestWorld rates and fees can be brought up during Council budget discussions.

Councilman Littlefield said the bottom line is that City policy since 1997 has always been to subsidize WestWorld to support the tourism industry. Mr. Dygert said they increased rates and fees slightly in the current fiscal year. This was based on the current configuration of the facility. They will begin to see the new rates and fees in the current budget cycle for FY 2013/2014, which will take into account the TNEC expansion.

Chair Klapp noted for the record that there were no disagreements in the audit report between the departments.

## **5. Discussion and Possible Direction to Staff direction to staff regarding Audit Follow-Ups, Second Quarter FY 2012/2013 Report**

Ms. Walker explained that the follow-up for audits generally involve minimal testing. She reviews the percentage of recommendations implemented plus those in progress. For this quarter, those two measures together total about 85 percent. At this time last year, they totaled about 88 percent. She reclassified several of the items that have been in progress for a prolonged period as partly implemented. The City's audit implementation statistics are comparable to other municipalities around the country.

**6. Discussion and Possible Direction to staff regarding 4th Quarter and Annual Taxpayer Problem Resolution Officer Report**

Ms. Davis presented the fourth quarter results. Taxpayer satisfaction remained very high.

The annual report shows that the Tax Audit Section mailed fewer surveys in 2012 compared to 2011. Although a lower percentage of audited taxpayers responded the rating were more favorable in 2012 than in 2011. The Tax and License Section consistently mailed 720 surveys each year. In calendar year 2012, more taxpayers responded than in the prior year. Ratings remain very positive.

Ms. Davis noted that in the third quarter one taxpayer had appealed to the TPRO. In the fourth quarter, the City Tax Collector issued a revised assessment for that taxpayer, and the taxpayer withdrew the protest. The auditors met with the taxpayer to discuss the process and address remaining questions.

**7. Discussion and Possible Direction to staff regarding status of FY 2012/13 Audit Plan**

Ms. Walker announced that the department is slightly ahead of schedule. She advised there will not be a need to meet in February.

**8 Discussion and Possible Direction to staff regarding agenda items for next Audit Committee meeting (March 18, 2013)**

Ms. Walker stated that the next meeting will be held on March 18.

Staff will present a report on case management controls, largely focusing on the City Prosecutor but also touching on the Police Department, the Court. The second audit is related to the City's costs for housing detainees at the County Jail. They will also report on the cost savings realized from new programs and procedures such as electronic monitoring and the in-jail court program.

Ms. Walker stated she plans to present a preliminary audit plan for FY 2013/2014, and provide an update on the status of her departmental budget.

In response to a query from Chair Klapp, Ms. Walker said that one member of the department has been on leave for several months but the Office is otherwise fully staffed.

**Public Comment**

No members of the public wished to address the Committee.

**Adjournment**



The meeting adjourned at approximately 4:56 p.m.

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